Supreme Court, U. S.
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In the Supreme Court
of the United States

OCTOBER TERM, 1977

No. 77-1694

BENJ. FRANKLIN FEDERAL SAVINGS AND LOAN ASSOCIATION, a corporation,

Petitioner,

v.

DERENCO, INC., a Nevada corporation,

Respondent.

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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INDEX

	Page
Opinion Below	1
Jurisdiction	2
Question Presented	3
Constitutional Provisions, Statutes, and Regulations Involved	3
Statement of the Case	3
1. The material facts	3
2. Federal regulations involved	4
3. State court proceedings	5
Reasons for Denying the Writ	7
1. The Decision of the Oregon Court is Clearly Consistent with the Decisions of This Court Applying the Doctrine of Federal Preemption to the Exercise of State Power	7
a. Preemption is not to be assumed or inferred in the absence of compelling reasons	7
b. Inference of preemption based upon conflict, inconsistency or frustration of purpose	9
c. Inference of preemption based upon requirements of national uniformity	11
d. Inference of preemption based upon "occupation of the field"	12
2. The Decision of the Oregon Court is Consistent with *Federal National Mortgages Ass'n* v. *Lefkowitz*, 390 F. Supp. 1364 (S.D. N.Y. 1975), the Only Other Reported Decision in Which the Doctrine of Federal Preemption Has Been Applied to a State Requirement That Interest be Paid on Reserve Funds	16
Conclusion	16

TABLE OF AUTHORITIES

Page

Cases

Allen-Bradley Local v. *Wisconsin E. Rel. Bd.*, 315 U.S. 740 (1942) 8

Bethlehem Steel Co. v. *New York Labor Rel. Bd.*, 330 U.S. 767 (1947) 8, 9, 10, 12, 13

Cloverleaf Butter Co. v. *Patterson*, 315 U.S. 148 (1942) 9, 12, 13

Derenco, Inc. v. *Benj. Franklin Federal Savings and Loan Association*, 281 Or. 533, 577 P.2d 477 (1978) 1, 2, 6, 7, 10, 11

Federal National Mortgage Ass'n v. *Lefkowitz*, 390 F. Supp. 1364 (S.D. N.Y. 1975) 16

Florida Avocado Growers v. *Paul*, 373 U.S. 132 (1963) 8, 9

Guss v. *Utah L.R.B.*, 353 U.S. 1 (1957) 13

Head v. *Board of Examiners*, 374 U.S. 424 (1963) 14

Hines v. *Davidowitz*, 312 U.S. 52 (1941) 10, 15

Jones v. *Rath Packing Co.*, 430 U.S. 519 (1972) 9

Kelly v. *Washington*, 302 U.S. 1 (1937) 9, 12, 13, 14

Linn v. *United Plant Guard Workers*, 383 U.S. 53 (1966) 10

Market Street R. Co. v. *Railroad Commission*, 324 U.S. 548 (1945) 3

Mintz v. *Baldwin*, 289 U.S. 346 (1933) 8, 13

Missouri P.R. Co. v. *Porter*, 273 U.S. 341 (1927) 13

Napier v. *Atlantic Coast Line R. Co.*, 272 U.S. 605 (1926) 8, 13

TABLE OF AUTHORITIES (Cont.)

Page

Northwestern B. T. Co. v. *Nebraska State R. Co.*, 297 U.S. 471 (1936) 8, 13, 14

Oregon-Waeshington R. & Nav. Co. v. *Washington*, 270 U.S. 87 (1926) 12, 13

Radio Station WOW v. *Johnson*, 326 U.S. 120 (1944) 2, 3

Ray v. *Atlantic Richfield Co.*, — U.S. —, 55 L. Ed. 2d 179 (1978) 9

Reid v. *Colorado*, 187 U.S. 137 (1902) 8

Republic Natural Gas Co. v. *Oklahoma*, 334 U.S. 62 (1947) 2

Rice v. *Santa Fe Elevator Corp.*, 331 U.S. 218 (1947) 8, 9, 13

Sand Springs Home v. *Naharkey*, 299 U.S. 588 (1936) 3

Savage v. *Jones*, 225 U.S. 501 (1912) 10

Smith v. *Illinois Bell Teleph. Co.*, 282 U.S. 133 (1930) 14

Statutes

12 U.S.C. §§ 1461 et seq 4

12 U.S.C. § 1464(a) 14

28 U.S.C. § 1257(3) 2

Oregon Revised Statutes § 13.380 2

Regulations

12 C.F.R. § 545.6-11, 23 F.R. 9902, December 23, 1958 ..... 5, 15

12 C.F.R. § 545.6-11(c), 40 F.R. 20942, May 14, 1975 ..... 5, 6, 7, 11, 12

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BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

Respondent herewith opposes Petitioner's petition for writ of certiorari to review the judgment of the Supreme Court of Oregon.

OPINION BELOW

The opinion of the Supreme Court of Oregon is reported at 281 Or. 533 and 577 P.2d 477. A copy of

the opinion is attached to the petition for writ of certiorari at page 23 as Appendix A.[1]

JURISDICTION

The judgment of the Supreme Court of Oregon was entered on March 21, 1978. Neither Petitioner nor Respondent petitioned for rehearing.

Petitioner erroneously contends that jurisdiction of this Court to review the judgment of the Supreme Court of Oregon by writ of certiorari is conferred by 28 U.S.C. § 1257(3). The statutory requirement of a final judgment has not been met, as the appeal to the Supreme Court of Oregon was interlocutory only, and the case has been remanded to the trial court for the purpose of initiating the accounting required by the court and proceeding to final judgment in the manner required by Oregon's class action statute.[2] Additional legal and factual issues will be determined in this process. This Court has in the past refused to assert jurisdiction over pending controversies until all legal and factual issues have been resolved, and not just those of overriding importance or of a federal nature. *Republic Natural Gas Co.* v. *Oklahoma*, 334 U.S. 62 (1947); *Radio Station WOW* v. *Johnson*, 326 U.S.

[1] The copy of the opinion set forth as Appendix A to the petition contains two errors at page 37. The fourth line of page 37 should read ". . . . that pursuant to valid statutory authority the Board . . . ." The fourteenth line should read ". . . . that the Board, and not the court, has primary juris— . . ." 281 Or. at 544 and 577 P.2d at 485.

[2] Oregon Revised Statutes § 13.380.

120 (1944); *Market Street R. Co.* v. *Railroad Commission*, 324 U.S. 548 (1945); *Sand Springs Home* v. *Naharkey*, 299 U.S. 588 (1936).

QUESTION PRESENTED

The single question presented for review is whether the common law of the state of Oregon, pursuant to which Petitioner was required to account for profits earned upon the tax and insurance reserves of its borrowers, was preempted by federal law by reason of the provisions of a Federal Home Loan Bank Board regulation which permitted federal savings and loan associations to require such reserve payments, but which contained no provisions with respect to the payment of interest upon such funds or the accounting for profits earned thereon.

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED

The constitutional provisions, statutes and regulations involved in this case are cited in the petition for writ of certiorari at page 3 and are set forth in Appendix C thereto at pages 77-80.

STATEMENT OF THE CASE

1. The material facts.

Petitioner is a federal savings and loan association chartered by the Federal Home Loan Bank Board

pursuant to authority vested in the Board by the Home Owners Loan Act of 1933.[3] In its role as a federal association, Petitioner is engaged in the business of making loans on the security of single family dwellings.

In addition to monthly payments of principal and interest, Petitioner's borrowers were at all material times required to make monthly payments of an amount estimated to be 1/12 of the annual amount of their real property taxes and insurance premiums. These reserve payments commenced a year in advance of the dates upon which payment of the taxes and insurance premiums was due. During the twelve month period of accumulation, Petitioner commingled the funds in its general account with other funds of the association and utilized them for investment and the generation of earnings which it retained and used for its own purposes. Petitioner subsequently paid the taxes and insurance premiums when due.

2. Federal regulations involved.

The primary regulation of the Federal Home Loan Bank Board pertaining to the real property security agreements used by federal associations is both mandatory and permissive in that it requires the inclusion of certain provisions in such agreements and permits the inclusion of others.

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[3] 12 U.S.C. §§ 1461 et seq.

Since 1958, the regulation[4] has in general terms required that such agreements provide the lender full protection with respect to insurance and taxes. In addition, it has permitted, but has not required, the collection of reserve payments. Until 1975 the regulation contained no provision of any kind with respect to the payment of interest upon such funds or the accounting for profits derived therefrom.

The regulation[5] was amended in 1975, however, and now requires the payment of interest on reserve funds held in connection with loans made on or after June 16, 1975, if state chartered associations in the state in which the subject dwelling is located are required to do so. The regulation further specifies that "except as provided by contract," federal associations shall have no obligation to pay interest on such funds.

3. State court proceedings.

Respondent initiated this suit in July of 1974 as a class action on behalf of all borrowers from Petitioner who made the above-described reserve payments. Respondent sought an accounting and the recovery of either interest on the borrowers' reserve payments at a reasonable rate or the actual profits realized by Petitioner as a result of its use of such funds.

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[4] 12 C.F.R. § 545.6-11, 23 F.R. 9902, Dec. 23, 1958. Set forth in Appendix C to Petition at page 79.

[5] 12 C.F.R. § 545.6-11(c), 40 F.R. 20942, May 14, 1975. Set forth in Appendix C to Petition at page 80.

After trial in the fall of 1975, the circuit court rejected Petitioner's argument that the regulations of the Board precluded the application of state common law with respect to the payment of interest or earnings and ordered Petitioner to account to its borrowers by paying interest upon their reserve payments at Petitioner's passbook savings rate in effect at the various times such payments were made. Shortly thereafter, the trial court certified its order for interlocutory appeal.

Subject to certain modifications,[6] the Supreme Court of Oregon affirmed the trial court's decision and remanded the case to the trial court for further proceedings. The court concluded that justice and fair dealing required a recovery by the borrowers[7] and that Petitioner would be unjustly enriched were it permitted to retain the proceeds resulting from its use of the funds.[8] Having considered the issue of preemption at length, the court held that there was no "substantial conflict or interference" between the decision of the trial court and the regulation of federal associations by Congress and the Board.[9] The court also concluded that prior to the promulgation of 12 C.F.R.

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[6] See note 6 of Petition at page 10.

[7] 281 Or. at 556, 577 P.2d at 491, Appendix A to Petition at page 53.

[8] 281 Or. at 557, 577 P.2d 491, Appendix A to Petition at page 54.

[9] 281 Or. at 541, 548, 577 P.2d at 483, 487, Appendix A to Petition at pages 32-33, 43.

§ 545.6-11(c) in 1975, the regulations of the Board had not "occupied the field" with respect to the payment of interest or earnings upon reserve funds and that state common law was not preempted.[10]

REASONS FOR DENYING THE WRIT

1. The Decision of the Oregon Court is Clearly Consistent with the Decisions of This Court Applying the Doctrine of Federal Preemption to the Exercise of State Power.

Petitioner contends that the Supreme Court of Oregon decided the federal question here involved in a way "probably inconsistent"[11] with this Court's decisions dealing with federal preemption. Although this Court has never ruled on the precise issue involved in this case, the Oregon court correctly decided the preemption issue by application of principles previously articulated by this Court. Petitioner's bold assertion that the Oregon court's decision "cannot withstand analysis under established principles of federal preemption"[12] cannot be sustained and is belied by a review of the decisions involved.

a. Preemption is not to be assumed or inferred in the absence of compelling reasons.

The settled mandate of this Court is that the judiciary must begin with the assumption that the exer-

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[10] 281 Or. at 541-542, 548, 577 P.2d at 484, 487, Appendix A to Petition at pages 33-36, 43.

[11] Petition, at page 10.

[12] Petition, at page 16.

cise of state power is not to be superseded or excluded by virtue of federal legislation unless that is the clear and manifest intent and purpose of Congress. *Florida Avocado Growers* v. *Paul*, 373 U.S. 132, 146 (1963); *Rice* v. *Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947); *Allen-Bradley Local* v. *Wisconsin E. Rel. Bd.*, 315 U.S. 740, 749 (1942); *Napier* v. *Atlantic Coast Line R. Co.*, 272 U.S. 605, 611 (1926); *Reid* v. *Colorado*, 187 U.S. 137, 148 (1902). See also *Northwestern B. T. Co.* v. *Nebraska State R. Co.*, 297 U.S. 471, 478 (1936) and *Mintz* v. *Baldwin*, 289 U.S. 346, 350 (1933). Since Congress can, if it chooses, unequivocally displace state power entirely, it needs no assistance in the form of generous judicial implication to achieve supersession of state authority, and any indulgence in construction should favor the exercise of state power. *Bethleham Steel Co.* v. *New York Labor Rel. Bd.*, 330 U.S. 767, 780 (1947) (Frankfurter, J., Separate Opinion).

Petitioner's contention[13] that state law cannot be applied to federal associations because of Congressional delegation of "unlimited authority" to the Board "without providing for that authority to be shared with the states" is completely contrary to the above-stated principles.

An explicit statutory declaration of preemption is but one way of expressing Congressional intent. In the absence of such a declaration, it must be determined

[13] Petition, at page 16.

whether the nature and subject matter of the federal legislation exclude the operation of state law. *Bethlehem Steel*, supra, at 72. Thus, whenever there is an assertion of implied preemption, the controlling question is the effect of the exercise of state power upon the regulatory scheme established by congress. *Cloverleaf Butter Co.* v. *Patterson*, 315 U.S. 148, 153 (1942). As a result the exercise of state power has been sustained except where it has conflicted with or frustrated the federal scheme, or unless from the totality of circumstances it has been determined that congress intended to occupy the field. *Ray* v. *Atlantic Richfield Co.*, — U.S. —, 55 L. Ed. 2d 179 (1978); *Jones* v. *Rath Packing Co.*, 430 U.S. 519, 525, 540-541 (1977); *Rice* v. *Santa Fe*, supra, at 230.

b. Inference of preemption based upon conflict, inconsistency or frustration of purpose.

The inference of preemptive intent is inescapable in those cases involving an actual conflict or inconsistency between state and federal law, rendering compliance with both an impossibility. *Rice* v. *Santa Fe*, supra, at 230; *Cloverleaf Butter*, supra, at 156; *Florida Avocado Growers*, supra, at 143-144. In order to justify an inference of preemption on these grounds, however, the repugnance or conflict must be so direct that the two cannot be reconciled or stand together, *Kelly* v. *Washington*, 302 U.S. 1, 10 (1937), and if the state law pertains to a matter which is merely peripheral to the concerns of the federal scheme, the

operation of state law will not be precluded, *Linn* v. *United Plant Guard Workers*, 383 U.S. 53, 61 (1966).

Preemptive intent has been inferred where the exercise of state power would prevent or stand as an obstacle to the accomplishment and execution of the full purposes and objectives of the federal act, or where its operation has been frustrated and its provisions refused their natural effect. *Bethlehem Steel*, supra, at 773; *Hines* v. *Davidowitz*, 312 U.S. 52, 67 (1941); *Savage* v. *Jones*, 225 U.S. 501, 533 (1912).

Petitioner contends that the Oregon court's decision presents a challenge to the Congressional plan of creating a national savings and loan system over which the Federal Home Loan Bank Board has exclusive and unlimited authority. Petitioner, however, has never described the manner or extent to which the application of Oregon law challenges, interferes with, or frustrates the purpose of the federal savings and loan system. Although the Oregon court hypothesized that the imposition of an accounting "could" produce an obstacle to the attainment of federal goals, it observed that "a considerable amount of speculation is required to entertain the possibility seriously."[14] It then concluded that "we do not believe that preemption occurs simply because under some imaginable set of economic facts the application of state law could

[14] 281 Or. at 541, 577 P.2d at 483, Appendix A to Petition at pages 32-33.

impede the efficient execution of a federal statutory purpose."[15]

Furthermore, Petitioner's contention that the payment of interest upon reserve funds presents a challenge to the Federal Home Loan Bank Board's supervision of savings and loan associations is contradicted by the Board's promulgation of 12 C.F.R. § 545.6-11 (c) in 1975, as a result of which federal associations are now required under certain circumstances to pay interest upon such funds. The Oregon court noted the contradiction and concluded that:

> "This action by the Board amounts to an administrative determination that imposition of a duty to pay interest does not in all situations result in the creation of an obstacle to attainment of the federal goals." 281 Or. 541, 577 P.2d 483-484, Appendix A to Petition at page 33.

Petitioner's statement that the "authority to supervise federal associations is no longer to be exercised exclusively by the Board, but will be broadly shared by each state"[16] is a gross exaggeration of the court's decision.

c. Inference of preemption based upon requirements of national uniformity.

Congressional action with respect to a subject in which the federal interest is dominant and which nec-

[15] 281 Or. at 541, 577 P.2d at 483, Appendix A to Petition, at pages 32-33.

[16] Petition, at page 14.

essarily and in all respects requires uniformity of regulation will justify an inference of preemption. *Kelly* v. *Washington*, supra, at 14-15; *Rice* v. *Santa Fe*, supra, at 230. It has long been recognized, however, that in those fields of commerce where uniformity is not essential, either state or federal laws may apply, *Cloverleaf Butter*, supra, at 155, especially if the regulated subject affects local business relations, *Bethlehem Steel*, supra, at 772.

Petitioner's misplaced reliance upon principles of national uniformity is demonstrated by the Board's promulgation of 12 C.F.R. § 545.6-11(c) in 1975. The Board's incorporation of state law to trigger the obligation of federal associations to pay interest on reserves is itself the antithesis of uniformity.

d. Inference of preemption based upon "occupation of the field."

When the regulation of an activity involves none of the foregoing considerations, concurrent state and federal regulation may occur, with state power directed towards those aspects of the activity which federal law and regulations have left untouched. *Cloverleaf Butter*, supra, at 155-156. See also *Kelly* v. *Washington*, supra, at 9-10, and *Oregon-Washington R. & Nav. Co.* v. *Washington*, 270 U.S. 87, 102 (1926).

At such time as federal regulation does occur, the preemptive nature of the regulation will vary in scope. Total preemption occurs in those situations in which

the federal regulatory scheme is so pervasive as to justify the inference that Congress left no room for the exercise of supplementary state power. *Rice* v. *Santa Fe*, supra, at 230. The same degree of preemption occurs in those cases in which a federal agency has not acted to the full extent of its authority, with such inaction having the character of an administrative determination that further regulation by state or federal authorities is neither necessary nor appropriate. See *Bethlehem Steel*, supra, at 774 and *Cloverleaf Butter*, supra, at 170 (Stone, C.J., Dissenting Opinion).[17] Contrasting these extremes, however, are a multitude of situations in which the exercise of state power with respect to a federally regulated activity pertains only to a distinct segment of the activity not yet specifically regulated by the federal agency. Until such time as that particular segment is specifically covered by federal regulation, the exercise of state power remains undisturbed. See *Bethlehem Steel*, supra, at 774. There is no constitutional rule which requires Congress or a federal agency to address all aspects of any given subject and thereby occupy the entire field. State regulation outside that given field is not preempted in the absence of conflict or inconsistency, see *Cloverleaf Butter*, supra, at 155-156, and *Kelly* v. *Washington*, supra, at 10, and there is no inconsistency when state laws touch that which federal laws

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[17] Compare *Guss* v. *Utah L.R.B.*, 353 U.S. 1 (1957) with *Northwestern B. T. Co.*, supra, *Mintz* v. *Baldwin*, supra, *Missouri P. R. Co.* v. *Porter*, 273 U.S. 341 (1927), *Napier*, supra, and *Oregon-Washington*, supra.

and regulations have left untouched, *Kelly* v. *Washington*, supra, at 13.

In support of its claim of preemption, Petitioner emphasizes the "sweeping terms" by which the Home Owners Loan Act of 1933 conferred broad powers upon the Board,[18] and cites authorities suggesting that such broad delegation of authority in connection with financial systems was unprecedented.[19] But this argument begs the question, since the exercise of state power is precluded, not as a result of the naked *grant* of power, but rather as a result of the *exercise* of such power. *Smith* v. *Illinois Bell Teleph. Co.*, 282 U.S. 133, 159-160 (1930). See also *Northwestern B. T. Co.* v. *Nebraska State R. Co.*, 297 U.S. 471, 478 (1936). Nor is the Board's promulgation of extensive and detailed regulations determinative, since the mere existence of such regulations cannot extend them beyond the boundaries they establish. *Kelly* v. *Washington*, supra, at 13. Claims of preemption cannot be judged by references to broad statements about "comprehensive" regulations. *Head* v. *Board of Examiners*, 374 U.S. 424, 429-430 (1963).

Petitioner contends that since 1958 the Board has actively "regulated" the subject of reserve accounts because it has not specifically permitted the payment of interest thereon. Petitioner submits that rather than constituting a regulatory gap to be filled by the

[18] 12 U.S.C. § 1464(a).

[19] Petition, at pages 11-12.

application of state law, the provisions of 12 C.F.R. § 545.6-11 were the result of an affirmative determination by the Board that it had provided all the regulation that was necessary and appropriate.[20] These contentions are without merit. First, mere authorization to maintain the accounts does not amount to active regulation with respect to all aspects of such accounts. Although the accounts were indeed authorized, there was no provision of any kind with respect to the payment of interest. Second, the logical extension of Petitioner's argument is that the Board intended to provide all the regulation that was necessary or appropriate with respect to the other provisions of 12 C.F.R. § 545.6-11 as well, thereby precluding the application of state law to an entire range of subjects, including the interpretation and effect of the terms of the notes, bonds and other real property security agreements used by federal associations.

Finally, little aid can be derived from the vague and illusory statement that federal regulations, by "occupying the field,"[21] have preempted the application of state law. Every act of Congress occupies some field, and the boundaries must be known and ascertained before a determination can be made that the exercise of state power is precluded. See *Hines*, supra, at 78-79.

[20] Petition, at page 17.

[21] Petition, at page 16.

2. The Decision of the Oregon Court is Consistent with Federal National Mortgage Ass'n v. Lefkowitz, 390 F. Supp. 1364 (S.D. N.Y. 1975), the Only Other Reported Decision in which the Doctrine of Federal Preemption Has Been Applied to a State Requirement That Interest be Paid on Reserve Funds.

At issue in *Lefkowitz* was a New York statute which required the payment of interest on reserve funds held by the mortgage association. The association contended that the payment of interest interfered with its federally mandated function and therefore violated the supremacy clause.

The court concluded that the burden imposed by the statute was insignificant and in no way interfered with the association's function of providing supplementary assistance to the secondary market for home mortgages. 390 F. Supp. at 1369. The court rejected the association's contention that the statute effectively dictated the internal administration of the association's funds and held that the impact of the regulation fell not upon the association, but upon the contractual relationship between mortgagor and mortgagee. 390 F. Supp. at 1370.

Although numerous courts have applied general principles of federal preemption to various regulations of the Home Loan Bank Board, no others have dealt with the precise issue here involved.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for writ of certiorari should be denied.

Respectfully submitted,

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